

## #40 CONTRACTORS

### An Educational Guide to Sales Tax in the State of Idaho

This brochure is intended to help contractors understand the sales tax laws that apply to their business. This information is based on the sales tax laws and rules in effect on July 1, 2005.

#### Who is a contractor?

A contractor is anyone who builds, improves, repairs, or alters *real property*, either commercial or residential. Contractors include prime contractors, general contractors, subcontractors, and “speculation” contractors. Speculation contractors build on property they own in anticipation of selling it later.

*Examples of contractors include:*

bricklayers	fence builders
electricians	carpet layers
land levelers	plumbers
mechanical contractors	roofers
window installers	landscapers
drywall installers	pump installers
garage door installers	painters
sheet metal contractors	well drillers
heating and air conditioning installers	

#### What if I do only residential repairs?

You are considered a contractor by Idaho law. The information in this brochure applies to you.

#### What is real property?

“Real property” basically refers to land and improvements or fixtures to the land.

Improvements or fixtures include things that are physically attached to the land or to other improvements. *For example*, a house and fence are both improvements to the land on which they are built. Improvements and fixtures also include things that are attached in such a way that they would be expected to be sold along with the land. *For example*, you would be expected to leave the light fixtures in a home you sold because they are attached to the property.

## What is the difference between a contractor, a retailer, and a contractor/retailer?

A **contractor** installs or attaches materials to real property. A **retailer** sells goods, but does not attach them to the real property. A **contractor/retailer** does both.

## How does sales tax apply to a contractor?

The sales tax law says that a contractor is the consumer of the goods he uses. Therefore, he must pay sales tax on all his purchases.

Contractors owe sales tax when they buy equipment, tools, and supplies used in their business. They must also pay sales tax when they buy building materials and fixtures. “Fixtures” include lighting or plumbing fixtures, furnaces, boilers, heating or air-conditioning units, refrigeration units, elevators, hoists, awnings, vaults, cabinets, counters, carpet, garage doors, water heaters, etc.

If a contractor makes purchases on which sales tax has not been charged, he must pay use tax. The contractor must get a use tax number from the Idaho State Tax Commission and file use tax returns. Use tax is imposed at the rate of 5%, the same as sales tax.

## What if the customer is exempt from sales tax?

Even if the customer is exempt from paying sales tax, such as a government agency, the contractor must still pay tax on his purchases.

## What if the customer has direct pay authority?

Some project owners may have been granted direct pay authority by the Idaho State Tax Commission. This means that they buy tangible personal property exempt from tax and, if tax is due, pay it directly to the state instead of to the supplier.

A contractor may not make exempt purchases using his customer’s direct pay authorization. This authority may not be transferred.

A contractor must pay tax on the materials he installs into real property even when project owners give him a copy of their direct pay authorization.

## What if the customer provides the job materials?

If a project owner buys materials for a job and pays sales or use tax, the contractor who installs these materials does not owe any additional tax. However, if the owner has not paid tax on the materials he provides to the contractor, the contractor must pay use tax on the value of those materials. This situation occurs most often when the contractor does work for a project owner who is exempt from paying tax, such as a nonprofit hospital, school, or government agency.

## If a contractor fabricates material for a job, how much tax applies?

If a contractor fabricates his job materials, the amount of use tax he owes is based on the value of the material at the time he first handles it for a specific project to improve real property. *For example*, if a contractor buys steel for a specific job and fabricates it for use on that job, he owes use tax only on the materials he has purchased.

However, if the contractor fabricates steel and puts it into a resale inventory for future use, he owes tax on the full value of the fabricated steel at the time he incorporates it into real property. That value is called the “fabricated value” and includes the cost of the materials plus the fabrication labor.

## Should a contractor charge sales tax on the materials he installs?

No. A contractor does not charge his customers sales tax. His bid should be high enough to cover any taxes he has had to pay on materials without itemizing sales tax on his bid. If he does charge sales tax, his customer can refuse to pay it.

*Example:* A cabinetmaker agrees to build cabinets and install them in a home. He bids the job for labor and materials. The materials cost him \$1,000. He must pay \$50 sales tax to his material supplier or, if the supplier does not collect Idaho sales tax, he must remit \$50 use tax to the state. When he bills his customer, he has a materials cost of \$1,050. He reimburses himself for his material costs (including the tax he paid), but he *does not* charge his customer sales tax.

The bill might read:

Job materials	\$1,050
Labor	\$3,000

## How does sales tax apply to a retailer?

A retailer must get a seller’s permit to collect and remit sales tax. A cabinetmaker who builds cabinets and delivers them to another contractor to install in a home is a retailer. As a retailer, the cabinetmaker must collect sales tax on the full retail sales price of the cabinets, including his labor to make them.

His bill might read:

Materials to build cabinets	\$1,000
Labor to build cabinets	\$2,500
Sales tax on \$3,500	\$ 175

## How does sales tax apply to a contractor/retailer?

Many contractors are also retailers. Plumbers, electricians, carpet layers, cabinetmakers, and mechanical contractors, to name a few, are usually both contractors and retailers. They are contractors when they install materials in the course of a residential or commercial service call or contract; but when they sell items or materials that they do not install, they are retailers and need to collect sales tax from their customers.

A contractor/retailer must ensure that the correct tax is paid. Since part of his materials will be subject to tax on cost (when he acts as a contractor), and part will be subject to the collection of sales tax (when he acts as a retailer), he must keep records that enable him to properly account for the tax.

A contractor/retailer may follow any consistent procedure that properly accounts for the tax due. *For example*, if the majority of a contractor/retailer's business is in retailing, he may want to buy all of his materials without tax by giving his supplier a completed form ST-101, Sales Tax Resale or Exemption Certificate. For more information on exempt sales, see Brochure #5 - Retailers and Wholesalers: Making Exempt Sales. When he retails the goods, he will collect sales tax. If he installs the materials into real property, he will owe use tax on the cost of the goods.

## Can any other methods be used to account for the tax?

If the majority of a contractor/retailer's business involves contracting, he may want to pay tax on all materials as he buys them. Then, if he installs the goods into real property, he has paid the sales tax and no use tax is due. If he sells goods at retail and collects sales tax, he will offset the sales tax due on his retail sales by subtracting the sales tax he paid to the vendor on the cost of the materials and then remit tax on the markup.

In another commonly-used method of recordkeeping, the contractor/retailer maintains a resale inventory purchased without paying sales tax, then pays use tax when materials are taken from inventory, and he pays sales tax when buying materials for major contracting jobs.

## How should I handle a contract where I'm both a contractor and a retailer?

*An example* of this is a cabinetmaker who contracts to build kitchen cabinets and a freestanding china hutch for a homeowner. If he installs the kitchen cabinets, he is acting as a contractor and owes tax on his material costs. But since the hutch is freestanding (not installed into real property), he is acting as a retailer and must collect tax from the homeowner on the retail sales price of the hutch (including his labor to build it).

When you are bidding a job with mixed contract services and retail goods, be sure to separate these on your invoice to the customer, and be sure to charge tax on the retail portion. *For example*:

Furnish and install kitchen cabinets		\$5,000
Build freestanding hutch	\$1,000	
Sales tax on hutch	\$ 50	
		<u>\$1,050</u>
Total		\$6,050

## Do contractors qualify for any exemptions?

A special exemption applies to contractors who are working in states with no sales tax, such as Montana, Oregon, and Alaska. Nonspeculation jobs in Washington also qualify for this exemption if the project owner is not the federal government. (In a nonspeculation job, the contractor does not own the real property.) A contractor does not have to pay tax on materials delivered to him in Idaho *as long as* those materials will be incorporated into real property on his job in a state with no sales tax. To claim the exemption, the contractor must complete form ST-101 and give it to the vendor.

A contractor who is fabricating production machinery for a production-exemption entity may make tax-free purchases of the materials that become part of the production equipment. He must give the vendor a completed form ST-101 for his records.

A contractor who is installing equipment used in agricultural irrigation, such as pumps and pipes, can buy these materials tax exempt. He must give the vendor a completed form ST-101.

A contractor who is an enrolled member of an Indian tribe with a job on the reservation may take delivery of materials on the reservation without owing sales or use tax. However, tax applies if the materials are delivered to the American Indian contractor off the reservation. A non-Indian contractor improving real property on an Indian reservation usually is subject to sales and use tax.

## Am I responsible for my subcontractor's sales or use taxes?

No. If you hire a subcontractor to furnish and install materials, he is responsible for the tax on the materials he buys.

However, if you buy the materials and hire a subcontractor to install them, you must pay the tax on the materials. If you don't, either you or the subcontractor can be held liable for the tax.

## Does a contractor have to pay tax when he applies rock?

A contractor who applies crushed rock is improving real property. If the contractor buys the crushed rock, he must pay tax on the purchase price. If the crushed rock is provided by the project owner or government agency that has not paid tax on the rock or the crushing services, the contractor owes tax on the value of the rock. The value is the "crushed value" (what a buyer would pay to a gravel pit owner for this type of crushed rock). If the contractor who applies the rock also crushed it, the value of the rock is the raw material cost (generally the royalty fee).

## Does a contractor have to pay tax when he crushes and stockpiles rock?

When a rock crusher contracts to crush and stockpile rock owned by another, he is not a contractor improving real property. Instead, he is a retailer of taxable processing services.

The rock crusher must obtain a seller's permit number and charge sales tax on his retail sale of crushing services (including mobilization fees). If his customer is exempt from paying sales tax, such as a state or federal government agency, no tax applies.

## What if the buyer of crushing services will resell the crushed rock?

If the rock crusher is crushing and stockpiling rock for a customer who will resell it, the services are not taxable if the buyer provides a completed resale certificate (form ST-101).

The rock crusher may qualify for the production exemption on his equipment, fuel, and certain supplies if the majority of his business is crushing rock that will be resold. This is true even if the crusher is not the owner of the rock. For more information on the production exemption and mining, see Brochures #30 - The production Exemption and #34 - Mining.

## Are subcontractors who work at the INEEL exempt from sales tax?

No. Subcontractors who improve real property at the Idaho National Engineering and Environmental Laboratory must pay tax on purchases for these projects, just as they would for other real property improvements.

## For more information, read:

Brochure #2	Use Tax
Brochure #5	Retailers and Wholesalers: Making Exempt Sales
Brochure #30	The Production Exemption
Rules 12, 13, 14, and 15	The Contractor Rules
Rule 16	Retail Sale of Asphalt, Concrete, and Concrete Products

### For more information, contact:

- Idaho State Tax Commission: In the Boise area, 334-7660; Toll free, (800) 972-7660
- Hearing impaired: TDD (800) 377-3529
- **tax.idaho.gov**

This information was prepared by the Idaho State Tax Commission. It does not provide comprehensive explanations of Idaho tax laws or rules. Specific questions should be addressed to the Tax Commission or a qualified tax practitioner.